United States Court of Appeals

for the Second Circuit

RESPONDENT'S BRIEF

No. 76-6040

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA and WALTER ROSS,
Revenue Agent, Internal Revenue Service,
Petitioners-Appellants,
Cross-Appellees,

v.

GEOFFREY DAVEY, As Secretary of THE CONTINENTAL CORPORATION,
Respondent-Appellee,
Cross-Appellant.

REPLY BRIEF OF RESPONDENT-APPELLEE-CROSS-APPELLANT

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Dated: Washington, D.C.
June 9, 1976

PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D. C.

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ARGUMENT I

THE DISTRICT COURT ERRED IN ORDERING COMPLIANCE WITH THE INTERNAL REVENUE SERVICE SUMMONS

Point I

The Questions Before This Court Are Essentially Questions of Law, Not of Fact.

The Government's reply brief urges affirmance of the District Court's enforcement order on the basis of the burden of proof on appeal.[1] Thus, the Government asserts that the District Court's findings of fact must be affirmed unless "clearly erroneous." (Gov't Reply, p. 7).[2] This standard is correct, but has no bearing on this appeal.

There is no question as to the Government's purpose in seeking these tapes. The I.R.S. wants to reprogram the tapes in order to "pull out" certain expenses over specified amounts, even though the same process could be readily performed from Continental's permanent books and records. The only questions on appeal are whether that purpose is a proper one, whether computer tapes are "books and records" within the meaning of Section 7602, and whether the Government has discharged its burden of proving that it has complied with the various conditions precedent to summons enforcement.[3] These are questions of law, and there is no presumption that the Government's interpretations of law are correct.

The District Court's determinations that computer tapes may be summoned under Section 7602 and that the convenience of the agents is a sufficient basis for summons enforcement also involve questions of law, not of fact. Continental does not have the burden of establishing that the District Court's decisions on questions of law were "clearly erroneous." *In Re Joseph Kanner Hat Co., Inc.*, 482 F.2d 937 (2d Cir. 1973); *Wirtz* v. *Barnes Grocer Com-*

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[1] In accordance with the practice followed in the earlier briefs on this appeal, the Petitioners-Appellants, Cross-Appellees, the United States of America and Walter Ross, will be referred to as the "Government" and Respondent-Appellee, Cross-Appellant, Geoffrey Davey as Secretary of the Continental Corporation, will be referred to as "Continental."

[2] The Government's reply brief dated June 2, 1976 will be cited (Gov't Reply, p.).

[3] The Government has the burden of proving it has complied with a number of conditions precedent, including proof that the information sought has not already been made available. *United States* v. *McCarthy*, 514 F.2d 368 (3d Cir. 1975).

pany, 398 F.2d 718 (8th Cir. 1968); *Kwikset Locks, Inc.* v. *Hillgren*, 210 F.2d 483, 488-89 (9th Cir. 1954), *cert. denied*, 347 U.S. 989; *cf. United States* v. *United States Gypsum Co.*, 333 U.S. 364, 396 (1948).

Point II.

The I.R.S. Is Seeking the Tapes to Serve Its Convenience and Not To Obtain "Data".

The Government's reply brief claims that computer tapes constitute "other data" within the meaning of Section 7602. (Gov't Reply, pp. 5-6.) However, the Government totally fails to deal with the crucial fact that the I.R.S. does not want the tapes to obtain the data contained in the electrons thereon. *All* of the data on the tapes has already been made available to the I.R.S. in visible and legible form in Continental's permanent books and records. (A-70, 88, 143.)[4]

Initially, the I.R.S. asserted that without the computer tapes an individual transaction could not be traced from the original documents to Continental's tax return. The hearing below established that this assertion was simply not true. Continental's permanent books and records, including the print-outs from the tapes in question, provide a complete "audit trail" from the original documents to the tax return. (A-102-103, 124-25.) The I.R.S. conceded at the hearing that it had audited Continental for a number of years without asking for the computer tapes. (A-124-25.) The tapes were not needed for audit purposes. (A-124-25.)

The I.R.S. also contended that the tapes were necessary because they contain payroll, commission and brokerage expense information not found on the print-outs. (A-33.) Again, this contention proved to be without factual basis. The summoned tapes themselves do not contain payroll,

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[4] The joint appendix on appeal will be cited as (A-).

commission and brokerage expense information. (A-92-93.)

Instead, the I.R.S. wants the tapes only to pull out certain expenses of more than specified amounts. (A-121-22.)[5] The Government attempted to introduce into evidence exhibits showing computer "stratifications" of legal fees that the I.R.S. had prepared with respect to another taxpayer. Government counsel explained that these stratifications—

> "show by clear example by the revenue agent before us, exactly the stratification of information grouping that he is searching in the Continental Corporation which has heretofore been denied by them." (A-119.)

The stratification can readily be obtained from the print-outs which are part of Continental's permanent books and records. (A-140-41.) The tapes are thus being sought solely to relieve the I.R.S. of a "tedious job." (A-127.) This showing of *convenience* to the I.R.S. agents does not satisfy the tests of *materiality* and *relevance* under Section 7602. *United States* v. *Matras*, 487 F.2d 1271 (8th Cir. 1973). All the *data* has been already made available.

The Government's reply brief seeks to divert attention from this crucial point by raising a number of false issues. The Government stresses that Continental has agreed that if the I.R.S. were to show some reason to doubt the accuracy of the print-outs, the tapes would be an appro-

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[5] The I.R.S.'s desire to have the tapes solely in order to reprogram and rearrange Continental's books and records, and not to obtain "data" not already made available, is made clear in the testimony of the Government's computer expert:

> "Well, inasmuch as the exact items and information on the printout are exactly the same as those same corresponding items of information on the tape, the information content may well be equivalent.
>
> "But there is this dimension of form. It is really extremely important. Talking about equivalent information sources, in these days of massive masses of data, it is no longer limited to content only. It has to be the form in which it exists." (A-143.)

priate means to verify whether the permanent books and records correctly reflect the information on the tapes. (Gov't Reply, p. 4). This does not support enforcement of the present summons, since the I.R.S. conceded at the hearing below that the accuracy of the print-outs was not in question. (A-139.)

The Government's reply brief asserts that the District Court found that the print-outs are "inadequate for I.R.S. audit purposes" and that only the tapes can provide an "audit trail" from the original documents to the tax return. (Gov't Reply, pp. 9, 5.) These assertions seriously misrepresent the District Court's opinion. The District Court found only that audit trails are "necessarily required" for the completion of an audit. There was no finding that the computer tapes are the essential means for following such audit trails. The opposite finding is implicit in the District Court's statement that the balance was "tipped" in favor of production because tracing the audit trails manually would require more work by the I.R.S. *United States* v. *Davey*, 404 F. Supp. 1283, 1284-85 (S.D. N.Y. 1975).

We believe the District Court to be in error because the summons power is not exercisable to impose a duty on the taxpayer to satisfy the convenience or limited time-saving objectives of the I.R.S.

Point III.

Computer Tapes Are Not "Books, Papers, Records, Or Other Data" Within The Meaning of Section 7602.

The Government asserts that the requirements of Section 7602 have been met by the conclusory statements of revenue agents that computer tapes are books and records. (Gov't Reply, p. 3.) Such statements are entitled to no weight on a question of statutory interpretation. The Government's reply brief further asserts that no authority supports the proposition that Section 7602 applies only to

"visible and legible records," and not to computer tapes. (Gov't Reply, p. 6.) The Government may be saying that the courts have never before applied Section 7602 to computer tapes. That statement is correct, but hardly supports enforcement of this summons. The Government may also be saying that there is no authority holding that the statutory language refers to visible and legible materials. That statement is not correct. Revenue Procedure 64-12, 1964-1 Cum. Bull. (Part I) 672, discusses in detail the statutory requirement that taxpayers must maintain books and records showing their tax liabilities. The I.R.S. there concluded that the statutory language was designed to ensure that "visible and legible records" will be available for I.R.S. inspection.[6]

In an attempt to fit computer tapes within the statutory language, the Government contends that the phrase "other data" in Section 7602 extends beyond visible and legible records. Indeed, anything would be "data," and any material the I.R.S. wished to examine would have to be produced, under the Government's theory. However, under the accepted canon of statutory construction of "ejusdem generis," the phrase "other data" must be limited to materials of the same class as "books, papers, records," *i.e.*, "visible and legible records" as the 1964 Revenue Procedure indicates. *Cleveland* v. *United States*, 329 U.S. 14, 18 (1946); *United States* v. *Stever*, 222 U.S. 167, 174 (1911); *Schwartz* v. *Romnes*, 495 F.2d 844, 849 (2d Cir. 1974).

The legislative history of Section 7602 is instructive on this point. Prior to 1954, the scope of the I.R.S. summons

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[6] The only contrary authority cited by the Government is Revenue Ruling 71-20, 1971-1 Cum. Bull. 392, which asserted, without citation of authority, that computer tapes are books and records. Revenue rulings, of course, reflect only the I.R.S.'s own views and have no more weight in interpreting statutory language, "than the opinion of any other lawyer." *Kaiser* v. *United States*, 262 F.2d 367, 370 (7th Cir. 1958), *aff'd*, 363 U.S. 299 (1960); *United States* v. *Bennett*, 186 F.2d 407, 410 (5th Cir. 1951); *cf. Bowers* v. *West Virginia Pulp & Paper Co.*, 297 F. 225 (2d Cir. 1924), *cert. denied*, 265 U.S. 584.

power was phrased in terms of "books, papers, records, *or memoranda.*" (Emphasis added). *See* Section 3614(a), 1939 Internal Revenue Code, 26 U.S.C. § 3614(a). The phrase "other data" was substituted for "memoranda" in 1954, but this reflected, as the Congressional Committees made clear, "no material change from existing law." H. Rep. No. 1337, 83d Cong., 2d Sess. (1954) p. A436; S. Rep. No. 1622, 83d Cong., 2d Sess. (1954), p. 617.

ARGUMENT II

THE DISTRICT COURT PROPERLY CONDITIONED ENFORCEMENT UPON PRODUCTION OF DUPLICATE TAPES AND REIMBURSEMENT BY I.R.S. OF THE COSTS OF DUPLICATION.

Point I

The District Court Properly Concluded That Duplication of the Tapes Was Necessary To Avoid Risk Of Damage.

The District Court found that Continental's computer tapes would be subject to risk of damage unless duplicates were made. As the Government concedes in its reply brief (Gov't Reply, p. 7), these findings of fact must be affirmed "unless clearly erroneous." *See, e.g., United States* v. *Zack,* 521 F.2d 1366, 1369 (9th Cir. 1975). The Government seeks to rebut the District Court's findings on this point by citing the Internal Revenue Manual ¶ 42 (13)1.7(3) for the view that the physical safety of the tapes will be safeguarded. The portion of the Internal Revenue Manual cited, however, merely states that unauthorized persons should not be given access to the tapes. No provision is made for protecting the tapes from physical damage.[7]

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[7] Internal Revenue Manual ¶ 42(13)1.6(8) lists certain precautions that are to be taken in shipping computer tapes. The Government's reply brief asserts that these precautions apply only to the I.R.S.'s own tapes, and not to taxpayers' tapes. (Gov't Reply, p. 13.)

Mr. George Moore, who has more than twenty-five years experience in the computer field, testified below that the tapes could be damaged if removed from their special protective storage facilities. (A-90.) The Government sought to discredit this testimony on cross-examination by quoting from an article in the *Journal of Accountancy*. Counsel for Continental did not obtain a copy of this article until after the hearing. Because of the Government's reliance on this published article in its original brief, Continental pointed out that the article in fact emphasized the careful steps required to prevent damage to computer tapes. The Government's reply brief now complains that Continental has gone outside the record by pointing out the true thrust of the published article relied upon by the Government. (Gov't Reply, p. 16). This complaint is without merit; if published materials may be used by the Government to assert half-truths, the Government should not complain if the taxpayer refers to the full contents.

Point II.

The District Court Properly Ordered I.R.S. Reimbursement Of the Costs of Duplication.

The Government's reply brief advances the novel theory that Continental must bear the costs of specially duplicating the computer tapes because it is a large corporation. (Gov't Reply, p. 14). Under the Government's theory, if it would be convenient for the I.R.S. to have an additional five copies of Continental's tax return, Section 7602 could be used to force Continental to bear the costs since they would not be large in relation to Continental's size. This theory must be rejected. Continental's size is irrelevant. The true question is what kind of costs and whose costs are involved. Where the purpose of compelling duplication of the tapes is to accommodate the revenue agents, the costs properly belong to the I.R.S.

The Government's reply brief argues that Continental must be required to bear the costs of duplication because these costs have been "established" to be $1,300. (Gov't Reply, pp. 13-14.) The size of the expense, like the size of the taxpayer, is irrelevant. Section 7602 cannot be used to compel Continental to provide a variety of facilities and services to the agents even though the costs might be far less than $1,300. The question still remains—whose expenses are involved? Furthermore, the $1,300 figure has no basis in the record of this case. That figure first appeared in a footnote to the Government's original brief on this appeal. It has now become an "established" fact in the record. As the Government concedes, "statements of counsel cannot bring into the record facts not disclosed by it." (Gov't Reply, p. 16.)

* * *

The Government's reply brief also contends that Continental's original brief has improperly gone beyond the record. The Government argues that Continental's statement of facts was based on affidavits not introduced into evidence.[8] (Gov't Reply, p. 15.) The facts set out in Continental's brief were originally contained in affidavits submitted in opposition to the enforcement of this summons. The same facts were then testified to by the affiants at the hearing below. Continental's brief referred to both the testimony at the hearing and the affidavits.[9] The statement of facts in Continental's brief would not have been changed in the least if the citations to the affidavits were omitted,

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[8] The affidavits were a part of the pleadings in the case, and therefore before the District Court. Moreover, the affiants as witnesses affirmed the correctness of the affidavits. (A-75, 94).

[9] In one or two instances, Continental's original brief on appeal cited a statement in the affidavits without giving the citation to the hearing transcript containing testimony to the same effect. For instance, page 5 of Continental's original brief describes the relationship of the print-outs to Continental's tax return. As the Government is perfectly aware, this point was the subject of extensive testimony at the hearing. (A-88-89, 102.)

although, since the affidavits are a part of the record, reaffirmed at the hearing, and subject to cross-examination, we know of no good reason why reference to them is precluded.

CONCLUSION

For the foregoing reasons, the District Court's Order requiring production of the tapes should be reversed. Alternatively, if the tapes are to be produced, the District Court's Order authorizing the taxpayer to produce duplicate tapes upon I.R.S. reimbursement of the reasonable and necessary costs of duplication should be affirmed.

Respectfully submitted,

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June 9, 1976

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REPLY BRIEF OF
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